

Annual Report Readership and Understanding: a Co-operative Perspective

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Abstract

This paper reports on a study of how members of a major New Zealand co-operative use their annual reports, addressing the dearth of accounting-based research in co-operatives. An important function of the annual report was seen to be giving members an indication of the value of the company and the fair value of their shares. Members read thoroughly both narrative and financial sections of the co-operative's annual report, yet readers perceived the most important information to be profit. There were differences between investor-owned companies (Lee & Tweedie, 1977) and co-operatives in importance placed on particular information and in which parts of the annual report were focused on.

Introduction

Lee and Tweedie (1975a, 1975b, 1977) initially examined the extent to which annual reports are read and understood by individual shareholders in the UK. Their main finding was that shareholders rely primarily on the narrative parts of annual reports. Twenty years after Lee & Tweedie, Bartlett & Chandler (1997) found that "little had changed" (p245) in the UK. By contrast, Epstein (1975) found that individual shareholders in the USA considered the financial statements to be more useful than narrative parts of the annual reports. A follow-up study, Epstein & Pava (1993), confirmed that shareholders do not perceive management discussion and analysis to be very useful. It also found that the annual report is believed to be more useful than twenty years before, profit statements are not as widely read, and auditors' reports are considered to be more important. An Australian replication (Anderson & Epstein, 1995, p26) found that "the directors' report was the most thoroughly read section of the annual report, followed by the profit and loss statement and chairman's report"; the auditors' report was the least useful and least read. Similar results were found in New Zealand, the most thoroughly read sections being, in descending order: the chairman's report, the directors' report, and the profit and loss statement (Anderson & Epstein, 1996).

Because members of co-operatives have transactional or trading relationships with their organisation it might be expected that the focus of co-operative members/shareholders will be different from that of investors in limited companies, who may be unskilled financially.

This study investigates the readership of annual reports by members of a New Zealand co-operative using a modified version of Lee & Tweedie's 1977 survey instrument.

The structure of the paper is as follows. The next section reviews the main research leading on from Lee & Tweedie's (1977) findings and its relevance to co-operatives. This is followed by the method used, the findings, discussion and a conclusion.

Prior literature

The seminal study of the use of annual reports was that of Lee & Tweedie (1977), which followed their pilot study, reported in two separate articles. Lee & Tweedie (1975a) examined whether or not shareholders use company financial report information and Lee & Tweedie (1975b) whether or not they understand it.

Since 1975 there have been several studies focusing on Lee & Tweedie's findings that shareholders rely mainly on the narrative parts of annual reports, such as the CEO's review. These studies, which examined either the content or the readability of the narratives, are listed and reviewed by Jones & Shoemaker (1994). However, they did not entirely replicate the coverage of Lee & Tweedie, as they focused only on the narrative part of the annual report.¹

Courtis (1982) found that, although annual reports were ranked third to stockbroker advice and newspapers as sources of corporate information, two-thirds of respondents claimed that the annual report was of some importance and one-quarter would be prepared to pay to receive a copy. Courtis (1982) also found that,

whereas the chairman's review was the most read item, traditional financial statements were more important in influencing equity decision-making. The auditor's report, statistical data and notes to the accounts were the least read and least important.

Some studies, such as Lee & Tweedie (1981), Chang & Most (1985) and Day (1986), widened the focus by considering whether different groups of investors (individuals, institutional investors and financial analysts) found periodic financial statements useful in their investment decision making. Chang & Most (1985, p38) found that "financial analysts as a whole placed greater importance on corporate annual reports than did institutional investors; institutional investors, in turn, placed greater importance on such reports than did individual investors". Chang & Most's (1985) findings suggest that similarly there could be differences between the responses of shareholders in different types of organisations.

Other work has focused on different aspects of the annual report. For example, Yuthas et al (2002) examined how companies strategically used their reports to release news. Rogers & Grant (1997) and Previts et al (1994) have taken a financial analyst's, rather than a shareholder's, perspective.

Since 1977, there have been many changes to the format of annual reports; for example, the cash flow statement is now required and narrative parts of the report are typically longer. Because of these changes, Bartlett & Chandler (1997) carried out a partial replication of Lee & Tweedie's 1970s studies. They found that in the UK "the annual report is still not widely read ... despite the significant changes in financial reporting" (p259). Similar results were found in Australia by Anderson & Epstein (1995). Epstein and Pava (1993) found that US investors did consider the annual report to be useful, that investors did not rely on narrative sections provided voluntarily by management, and that the auditors' report was important to readers.

The studies cited all involved investor owned companies. Hyndman et al (2004) have analysed the quality of financial statements of Irish credit unions. Westerdahl's (2001) ethnographic study of a rural co-operative in Sweden concluded that figures presented in financial statements "are seen as difficult to grasp and interpret in light of the intuitive understanding of the problems" (p66), and "figures from the accounting systems generally

are not perceived as relevant to the activists and board members" (p67). However, no study has been made of the use and understanding of financial statements by individual members of co-operatives comparable to the Lee & Tweedie studies.

The co-operative form of organisation has a low profile because few co-operatives have shares which may be held by investors. It can, however, be a significant contributor in an economy. In New Zealand the twenty largest businesses include six co-operatives. The turnover of the top 20 businesses is over NZ\$55 billion; the six co-operatives generated over \$21 billion or 39% of that revenue ('Top 200 ...', 2002). In the 2001-2002 financial year New Zealand's largest co-operative, Fonterra Group Ltd, generated \$13.9 billion in revenue and had 13,000 shareholders. Other large co-operatives include: Ravensdown (turnover \$469 million in 2003, approx. 23,000 members), Farmlands (turnover \$250 million, approx. 14,000 members), Ashburton Trading Society (turnover \$105 million, approx 2,000 members) and Foodstuffs Group, comprising Foodstuffs Auckland Ltd (turnover \$2,596 million, 184 grocery members), Foodstuffs (Wellington) Co-operative Society Ltd (turnover \$1.547 million, 171 grocery members) and Foodstuffs (South Island) Ltd (turnover \$1,607 million, 374 grocery members plus 998 food service members).

The co-operative ethos has long involved recognition of accountability to members. In 1844 the Rochdale Equitable Pioneers Society required members to be supplied with quarterly audited accounts (Birchall, 1994). Today the International Co-operative Alliance (1995) states:

Co-operatives are democratic organisations controlled by their members, who actively participate in setting their policies and making decisions. Men and women serving as elected representatives are accountable to the membership. (<http://www.coop.org/ica/info/enprinciples.html>).

There is some evidence of reports falling short of full disclosure on the grounds of competitive disadvantage, even where the co-operative may be large. The Mondragon group of co-operatives in Spain comprises 166 co-operatives covering industrial, educational, housing, agricultural, services and retail sectors. Together they employ 21,000 workers (Birchall, 1997), yet their annual report has been

described as “apparently always ... reticent about disclosing information about performance” (Davidmann, 1996).

By contrast, the Co-operative Bank in Britain is recognised as a leader in accountability in the widest sense. It, and its sister organisation Co-operative Insurance Society, were the first in their respective sectors to introduce fully audited ‘triple bottom line’ (social, environmental & financial) reports in the UK² (Co-operative Financial Services, 2004).

The accountability of co-operatives to their members is widely recognised around the world as a longstanding practice and not an abstract notion:

Co-operatives ... are a global force, with 800 million members worldwide, yet at the same time major local actors with a capacity which is built on trust and accountability (WCSDG, 2004, p69).

Although co-operatives are a major contributor to the economy, this organisational form has received little research attention, nor any research on the use of annual reports by members of co-operatives. This research seeks to redress this imbalance by examining the readership of annual reports by members of a supplier co-operative.

Method

A questionnaire was developed based on Lee & Tweedie (1977). Only a small number of changes were required to ensure that it was applicable to the co-operative sector. For example, ‘rebates’ was used rather than ‘dividends’. Questions about investment decisions were omitted as shares in this co-operative were membership shares and not investment shares. Contemporary financial report content and terminology was used; for example, ‘statement of cash flows’ replaced Lee & Tweedie’s references to ‘funds statements’. The questionnaire is reproduced in the Appendix.

Foodstuffs (South Island) Ltd was chosen as the co-operative to study because it is a significant and successful entity in a very competitive sector of the economy. It is a co-operative which is owned by independent grocers who trade under four banner groups ranging from small ‘corner store’ businesses to ‘warehouse-type’ supermarkets. In addition to purchasing in bulk from manufacturers the co-operative also produces a range of own-

brand products for its members. The co-operative has extensive property investments in warehouse, supermarkets and shopping mall complexes. It also acts as a financier taking deposits from and lending to its shareholders and the public. The co-operative offers a substantial degree of assistance to its members in the marketing of their business and products (Foodstuffs Annual Report 2003).

In this co-operative, 109 shareholders owned ‘A’ voting shares. Voting shares are allocated only to banner group members of five years or more standing with weekly purchases exceeding \$7,500. The remaining 265 grocery members and 998 food service members held ‘B’ redeemable preference shares which confer membership but not voting power³. Access to the membership was made possible because the senior management was interested in knowing whether the annual reports were providing a service to members.

Questionnaires were mailed to the entire population of 109 voting shareholders. In the initial mailing, the questionnaires were accompanied by a letter from Foodstuffs encouraging members to respond. Three respondents indicated that they should not be included in the survey (two had ceased trading; the other was a holding company), giving a population of 106. There were 25 responses from the first mailing. Four weeks later a follow-up letter was sent to non-respondents, eliciting a further 24 responses. Thus the overall response was 49 (46%). This is a favourable response rate, as “mail surveys with a return of about 30 per cent are often considered satisfactory” (Cooper & Emory, 1995, p282).

Results and interpretation

Descriptive statistics

The Foodstuffs’ members’ businesses range from corner store grocers to large supermarkets. In consultation with the company secretary, the Foodstuffs’ members were classified into three size categories according to weekly turnover. Details of responses in each category are shown in Table 1.

The individual respondents had been in the grocery business on average for 19.8 years (ranging from 7 to 45 years). Their business background and experience is shown in Table 2.

Two (4%) of the 49 respondents had a considerable background and experience with accounting (ie an accounting qualification), 39

Size	Criteria for classification	Number of responses	%
Large	Turnover \$1 million per week and over	5	10%
Medium	Turnover \$200,000 to \$1,000,000 per week	16	33%
Small	Turnover under \$200,000 per week	28	57%

Table 1: Relative size of respondent companies

Background & experience	Number of responses ⁶
Accounting qualification	2
Courses in accounting	13
Basic bookkeeping experience	27
Management qualifications	13
Foodstuffs' training courses	19
Other qualifications	6
Directorships	13
Other	10
None	5
	(n=49)

Table 2: Business background

(81%) had some experience with accounting (courses in accounting, 27%; basic bookkeeping experience, 56%; management qualifications, 13%; Foodstuffs' training, 19%; or directorships, 13%)⁴; the remaining 5 (10%) had no accounting experience.

Eight per cent of respondents had investments in 20 or more companies other than Foodstuffs, 14% had investments in between 6 and 20 other companies, 33% had investments in 1-5 other companies, and 45% had no other investments.

Important financial information

In response to an open-ended question, "What particular financial information about Foodstuffs is important to you?", members listed a range of items. These have been classified into 13 categories, in descending order of frequency, in Table 3. A comparison is made with responses in the Lee & Tweedie (1977) study where applicable.

Consistent with Lee & Tweedie (1977), profitability is the most important information for the respondents in both investor owned firms

	Number of responses ⁷	%	Lee & Tweedie (1977)
Profits/earnings	19	54%	52%
All information	11	31%	-
Rebate information ⁸	10	29%	36%
Assets	9	26%	9%
Sales & turnover	7	20%	12%
Future prospects	5	14%	18%
Share price	N/A	N/A	12%
Profits trend	2	6%	9%
Cash/liquidity	2	6%	7%
None	2	6%	-
Capital base (shares, reserves)	1	3%	12%
General trends	0	0%	6%
Other	2	6%	-
	n=35		n=301

Table 3: Important financial information

Section	Read thoroughly		Read briefly		Do not read		n
	No	%	No	%	No	%	
Highlights	23	51%	17	38%	5	11%	45
Directors and Executives (details)	21	49%	16	37%	6	14%	43
Directors' Report	21	46%	19	41%	6	13%	46
Foodstuffs Community Trust Report ⁹	12	29%	22	52%	8	19%	42
Corporate Governance	5	13%	16	42%	17	45%	38
Statutory Information	6	15%	14	36%	19	49%	39
Auditors' Report	9	21%	22	51%	12	28%	43
Statement of Financial Performance	23	51%	15	33%	7	16%	45
Statement of Movements in Equity	14	36%	14	36%	11	28%	39
Statement of Financial Position	23	53%	13	30%	7	16%	43
Statement of Cash Flows	18	45%	12	30%	10	25%	40
Notes to the financial statements	12	27%	22	50%	10	23%	44
National Progress Report ¹⁰	17	40%	18	42%	8	19%	43
Directory	8	21%	19	50%	11	29%	38

Table 4: Reading of the Annual Report

and co-operatives (52% and 54% respectively). Many in this study (31%) said that **all** information was important. This category did not appear in Lee & Tweedie (1977). There are also major differences between the two studies in the importance placed on information regarding assets, sales and turnover (these being more important in this study), and rebates/dividends and the capital base (these being more important in Lee & Tweedie, 1977).

Thoroughness of reading of the annual report

The questionnaire asked which sections of the annual report were read and how thoroughly. Following Lee & Tweedie (1977), a rating of 2 was assigned to "Read thoroughly", 1 to "Read briefly for interest", and 0 to "Do not read at all". Percentages in each category are presented in Table 4.

The most thoroughly read section of the annual report was the Statement of Financial Position (Balance Sheet) (53%), followed by the

Highlights and the Statement of Financial Performance (Profit and Loss) (51%), then details of Directors and Executives (photos, names and details) (49%), the Directors' Report (46%) and the Statement of Cash Flows (45%). These findings contrast significantly with Lee & Tweedie (1977) where the Chairman's Report was read thoroughly by 52% of respondents; other sections ranking highly in this study had a much smaller readership in Lee & Tweedie (1977), as shown in Table 5. Possible reasons for this are discussed later.

Following Lee & Tweedie (1977), respondents were classified according to the thoroughness of their reading of reports. Ratings of 2, 1 and 0 were summed for the 14 parts of the annual report, giving a possible maximum score of 28. Scores of 18 and above (including at least three of the four financial reports) were categorised as "thorough readers" (35%); below 18 were classified as "less interested readers" (53%). Six respondents

Section	Read thoroughly	Lee & Tweedie (1977)
Statement of Financial Position	53%	29%
Highlights	51%	-
Statement of Financial Performance	51%	39%
Directors & Executives	49%	-
Chairman's Report ¹¹	-	52%
Directors' Report	46%	27%
Statement of Cash Flows ¹²	45%	18%
Notes to the Financial Statements	27%	21%
Statistical Data ¹³	-	19%
Auditor's Report	21%	16%

Table 5: Comparison of Thorough Reading of Sections of the Annual Report

(12%) did not read any part of the annual reports. There were three reasons given: lack of interest (5), lack of time (4), and difficulty in understanding it (2). Lee & Tweedie (1977) reported only the numbers of thorough and less interested readers; if non-readers are left out, comparable percentages are 24% thorough in Lee & Tweedie (1977) (this study 40%) and 76% less interested (60%). The thoroughness score is used in tests presented later in the paper.

Analysis of data in reports

Although 7 respondents (6 or 33% of the thorough readers and one of the less interested readers) said they undertook some analysis of the data contained in the reports, 5 of them only compared results with the previous period (5 of those who carried out some analysis). One respondent occasionally asked an accountant to explain certain issues, and another worked out ratios of gross profit to turnover and rebates returned to members. However, this low level of analysis may be a compliment to the readability and amount of material voluntarily disclosed in the report (eg, information about rebates and the Foodstuffs' Community Trust). Alternatively, it may indicate that co-operative members merely use the annual report to check what they already know from trading continuously with Foodstuffs.

The purpose of financial statements

When asked about the purpose of the financial statements in the annual reports, the purpose ranked first or second by a majority of the respondents was "To give members an indication of the value of the company" (68%), and second was "To make directors accountable to members" (63%). All percentages are shown in Table 6.

It is surprising that 43% of respondents think that financial statements give them an indication of the fair value of their shares. Shares in this co-operative are issued and redeemed at nominal value rather than at a varying or 'fair' value, as is the normal practice in co-operatives; shares are membership instruments, rather than investment instruments.

Sections of the annual report

As shown in Table 7, the most important sections of the annual report (ranked 1 or 2) were the Statement of Financial Performance (ie Profit and Loss, 83%, compared with 68% Lee & Tweedie, 1977); the Statement of Financial Position (ie Balance Sheet, 74%, only 37% in Lee & Tweedie, 1977), the Statement of Movements in Equity (32%) and the Statement of Cash Flows (31%, 9% in Lee & Tweedie, 1977).

Although 83% of respondents believe that the financial information given in Foodstuffs' annual report is sufficient for members, there were some suggestions of additions to the information. Twenty-four per cent of respondents indicated that profit forecasts should be included, 16% wanted budgets, 8% wanted more details on human resources and 8% wanted environmental information. Two wanted "an expanded breakdown of some items, such as the purchases, wages and expenses" in the Statement of Cash Flows, and another wanted "some ratios on financial performance, stock turn etc" with an explanation of "what they mean".

Respondents felt they could realistically assess profitability (91%), capacity to survive (49%), managerial efficiency (44%) and investment policy (26%) from the present type of annual report.

Purpose	Ranking						n
	1	2	3	4	5	6	
To give members an indication of the value of the company	56%	12%	23%	5%	2%	2%	43
To make directors accountable to members	51%	12%	9%	19%	9%	0%	43
To give members an indication of the fair value of their shares	29%	14%	33%	19%	5%	0%	42
To justify rebates to members	29%	13%	24%	9%	18%	7%	45
To give members data useful for investment decisions	19%	10%	14%	12%	31%	14%	42
To provide information for the Inland Revenue Department	8%	3%	10%	8%	23%	48%	40

Table 6: Purpose of financial statements

Section	Ranking														n
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	
Statement of Financial Performance	58%	25%	8%	3%	0%	3%	0%	0%	0%	0%	0%	3%	3%	0%	40
Statement of Financial Position	51%	23%	18%	0%	3%	3%	3%	0%	0%	0%	0%	0%	0%	0%	39
Statement of Movements in Equity	24%	8%	19%	14%	0%	5%	0%	8%	5%	3%	0%	0%	8%	0%	37
Statement of Cash Flows	26%	5%	24%	21%	8%	0%	3%	3%	5%	0%	3%	0%	3%	0%	38
Directors' Report	26%	0%	5%	23%	13%	15%	8%	3%	0%	3%	3%	0%	3%	0%	39
Highlights	23%	0%	5%	10%	10%	5%	18%	3%	10%	5%	5%	3%	3%	0%	39
Directors and Executives	18%	5%	8%	5%	13%	5%	8%	10%	10%	8%	10%	0%	0%	0%	39
Auditors' Report	21%	0%	3%	6%	15%	6%	6%	6%	6%	9%	12%	3%	3%	6%	34
Notes to the financial statements	19%	0%	6%	6%	17%	17%	6%	6%	6%	8%	6%	6%	0%	0%	36
Statutory Information	14%	0%	3%	0%	6%	6%	8%	6%	6%	14%	17%	11%	6%	6%	36
Corporate Governance	11%	3%	0%	0%	8%	6%	8%	14%	6%	14%	14%	11%	6%	0%	36
Foodstuffs Community Trust Report	11%	3%	0%	0%	5%	3%	8%	5%	3%	19%	22%	3%	16%	3%	37
National Progress Report	9%	3%	0%	0%	12%	9%	12%	6%	6%	9%	15%	3%	12%	6%	34
Directory	6%	0%	0%	3%	6%	3%	3%	0%	0%	12%	18%	9%	12%	27%	33

Table 7: Relative importance of each section of the Annual Report

Reading of other sources of information about companies

The main sources of information about companies are presented in Table 8, together with the thoroughness of reading by the respondents. Other sources of information mentioned by respondents included television business programmes, the internet and share brokers' newsletters.

The most thoroughly read source of company information was local newspapers (38%). Company reports and trade magazines were the next sources, but were read thoroughly by only 17% to 21% of the respondents. These results cannot be compared with Lee & Tweedie (1977), who were asking about company annual reports as the main part of their study, and who listed different sources of information than those used in New Zealand. Also, there is no NZ equivalent of the daily financial press such as *The Financial Times* which featured strongly in the Lee & Tweedie (1977) study (with 54% thorough readership). In NZ the local newspapers are the only daily source of print information about financial issues. The *National Business Review*

and *The Independent* are weekly publications, and may be less readily available to the respondents outside the main population centres.

Reasons given for not reading the above sources of information about companies included: lack of time (5), lack of interest (5), reliance on advisors (2) and lack of understanding (1).

The information sought in the above sources is summarised in Table 9.

Understanding

Respondents were asked to explain some terms commonly used in financial reports: depreciation, movements in equity, current assets, foreign currency translation, minority interests, and derivative financial instruments. They were also asked what financial data they used to assess profitability, capacity to survive, managerial efficiency and investment policy. Each response was rated, by all three researchers and cross-checked by a colleague, on a scale of 2 (showing reasonable understanding), 1 (vague) and 0 (showing no understanding), following Lee & Tweedie (1977, p43).

	Six monthly financial reports	Weekly business press	Local newspapers	Trade magazines	Percent-ages	Lee & Tweedie (1977)
General Information	1	7	15	10	31%	18%
Financial reports	9	1	1	0	19%	15%
Share price	0	2	6	0	13%	15%
Future oriented information ¹⁴	5	0	1	7	15%	21%
Trends	5	1	0	2	10%	8%
Performance measures	0	4	5	1	10%	5%
Dividends	0	0	0	0	0%	5%

Table 9: Information derived from sources other than annual reports

Respondents were also asked how accurately the financial reports reflected Foodstuffs' progress and position. Only responses of "approximate" were deemed correct (rated 2), as in Lee & Tweedie (1977, p34), because "in preparing accounting reports, accountants are required to make a large number of accounting policy choices and also make estimates and approximations in arriving at most of the figures appearing in the financial statements" (Carnegie et al, 1997, p47). Other responses were rated 0.

Responses were summed, with a maximum possible score of 22. This score is the "understanding index" (Lee & Tweedie, 1977), which is used in the following analysis.

Correlation analysis

Relationships between variables were analysed using Pearson correlation analysis. Similarities and differences in findings between Lee & Tweedie (1977) and this study are detailed below.

Lee & Tweedie (1977, p78) concluded that "respondents who were thorough readers of annual reports had a substantially better understanding of reporting practice than less interested readers". This research supported that conclusion: thorough reading was positively correlated with understanding ($r=0.456$, $p=0.001$) and brief reading was negatively correlated with understanding ($r=-0.315$, $p=0.027$).

Lee & Tweedie (1977) found no relationship between size of investment and understanding of reporting practice. This study supported this finding.

Lee & Tweedie (1977, p79) found support for their hypothesis that respondents with significant accounting training "were more thorough readers of annual reports, and had a substantially better understanding of reporting practice, than those with little or no experience". There was no evidence of such relationships in this research. However, the population surveyed is different from that in Lee & Tweedie's (1977) study. To be a member of Foodstuffs, it is necessary to be actively involved in the grocery business. Lee & Tweedie's (1977) population, on the other hand, included shareholders not involved in business, such as housewives (11% of respondents), and their 'other' category (51%) inevitably included people without business experience, such as those who inherited their shares.

Lee & Tweedie (1977, p79) found that "respondents who read from several financial press sources were more thorough readers of annual reports, ... than those who made little or no use of the financial press". This study did not find this relationship. However, Foodstuffs is not a listed company, and the only comment in the media on its results is an annual press release from the co-operative itself. This may explain why respondents who thoroughly read the Foodstuffs annual report did not necessarily also read other financial press sources.

Lee & Tweedie (1977, p91) also found that "the more the financial press was read, the more likely its readers were to have higher than average understanding". This study also found that those that read three or more other sources had a higher understanding ($r=0.332$, $p=0.020$).

Lee & Tweedie (1977, p75) found that "respondents who did not read annual reports at all, or read them only briefly" also did not read other sources of financial information. This research found similar results. Those who did not read annual reports, also did not read any other sources ($r=0.684$, $p=0.000$). Brief readers read only one other source ($r=0.351$, $p=0.013$).

Lee & Tweedie (1977, p82) concluded that there was little relationship between the number of companies in which they held shares "and the extent of their readership of annual reports". This study, however, found that those with a medium portfolio (6-20 other companies) were thorough account readers ($r=0.315$, $p=0.027$) and those with no other investments did not read any other sources ($r=-0.376$, $p=0.008$).

Respondents from small firms did not read other sources ($r=-0.458$, $p=0.001$), they were not thorough account readers ($r=-0.408$, $p=0.004$) and they showed low understanding ($r=-0.383$, $p=0.007$). These small owner-operators may have little time or opportunity to read thoroughly and widely.

Respondents from small firms are also likely to have no other investments ($r=0.284$, $p=0.048$). This absence of investment in other firms is also not surprising, as Foodstuffs accepts deposits from members and associated traders, and pays interest at an above-market rate. For example, in the 2003 Annual Report, there was \$75.1 million on deposit from members and \$31.3 million from others, attracting "interest rates of up to 6.25%" (p 31), compared to a rate of 5.25% from banks at that time. These owners of small corner-grocery-type stores would have most of their money

tied up in their business, and would be likely to put any spare cash into their own co-operative.

Discussion

As was indicated earlier, it was expected that responses would be different from those found by Lee & Tweedie (1977). Some would be due to changes in the content of annual reports in the past 25 years, some to the nature of co-operatives in contrast to investor-owned firms and yet others to the particular features of this co-operative.

The respondents in this study placed differing levels of importance on financial information. More importance was placed on sales/turnover and assets in this study, and less importance was placed on rebates/dividends and the capital base.

The disclosure of sales or other gross operating revenues was recommended in New Zealand by the Macarthur Report in 1973 and by the accounting profession in 1976 (Pope & Burns, 1976). Following the international standard of the day, disclosure of sales was part of *SSAP-9: Information to be disclosed in company balance sheets and profit and loss accounts*, which came into force from 31 March 1979. However, accounting standards did not become part of legal reporting requirements until the passing of the Financial Reporting Act 1993. Similarly in the UK, where Lee & Tweedie carried out their studies, the Companies Act 1989 gave legal recognition to accounting standards. This may be one reason why respondents in Lee & Tweedie (1977) placed less importance on this information, as it was less frequently disclosed.

In a similar way, assets were frequently left at historical cost in Lee & Tweedie's time. Today revaluation of assets is encouraged "in order to provide more relevant information to users" (Institute of Chartered Accountants of New Zealand, FRS-3: Accounting for property, plant and equipment, section 7.2). Accordingly, readers today can expect the reported assets to be a more accurate reflection of current value.

Possibly the emphasis placed on turnover and assets is also driven by the fact that the respondents in this study were all active business people, for whom the link between assets and turnover is very real. In their own businesses, every dollar invested in assets must generate additional sales. Shareholders in investor owned firms, on the other hand, may

be less aware of this fundamental link. The Lee & Tweedie (1977) study identified only 38% of the respondents as being actively involved in business, whereas 100% of those in this study are. This suggests that care should be taken to recognise that there are different classes of 'users' of financial reports, just as there are different types of shareholders in the marketplace – speculators and investors (Chambers, 1974, p40).

Information about rebates and dividends was of less importance, possibly because of the frequency of contact which members have with their co-operative. For example, a Foodstuffs' member is likely to be dealing with Foodstuffs on a daily or weekly basis, and getting rebates monthly in cash, confirming the on-going performance of the co-operative. Not all co-operatives would be in a position of such regular and frequent contact with the members as is Foodstuffs. A fertiliser co-operative, for example, would be unlikely to have weekly dealings with its members, because purchases would be infrequent and seasonal. Also it could conceivably be paying rebates only at the end of the financial year. Further research will establish whether the findings of this study hold true for other types of co-operative.

As shown in Table 5, there were substantial differences in which parts of the annual report respondents focused on. In this study, respondents read all parts of the annual reports more thoroughly than in Lee & Tweedie (1977). The low readership of the Directors' Report in the Lee & Tweedie (1977) study is understandable when one appreciates that at that time the content of a directors' report was limited to any changes to the nature of the company's business, the recommended dividend, and any transfers to reserves⁵. Where there had been no material change in the nature of the company's business the report often took up less than half a page. This was so even when the directors supplemented the report with details of the proposed dividend, transfers to reserves, the names of directors who retired by rotation and the announcement that the auditors again offered their services. At that time, a comparable situation existed in New Zealand (*Companies Act 1955*, s161). However, the New Zealand Companies Act 1993 abolished the requirement for a separate directors' report. Consequently the content of the Directors' Report is now based on what the directors believe to be of

importance to members. The higher readership suggests that the information now included in the Directors' Report is of more interest to members.

The low readership of the "Sources and Application of Funds Statement" in Lee & Tweedie (1977) was possibly due to the fact that this statement was not seen as producing understandable information. 'Funds' were frequently not defined and were capable of many different definitions and several different titles (Beams & Strawser, 1973; Buzby & Falk, 1974; Heath, 1978). The Funds Statement was replaced by the Statement of Cash Flows in 1991 in the UK and in 1987 in NZ. The higher readership suggests that it is more relevant and more easily understood by readers than its predecessor.

There are two possible explanations for the significantly higher readership of the financial statements. Firstly, it is self-evident that the graphical standard of annual reports has changed: they are now more attractively presented, with photos, graphics, colour and different fonts. Therefore reports generally are now much easier to read. Secondly, members have regular dealings with their co-operative during the year, unlike shareholders in an investor-owned firm. They are more likely to want to know how 'their' business has been performing.

There is a difference between the two studies in relation to thoroughness of readership of the annual report; there were a higher percentage of thorough readers in this study. This may be due to Foodstuffs' practice of sending members a letter prior to the release of the annual report. This letter summarises and highlights the year's results in a non-technical form, which may encourage members to read the annual report.

As in Lee & Tweedie (1977), the most important sections of the Annual Report are the Balance Sheet and the Profit and Loss Statement. The other financial statements are also very important, and all the financial sections are of higher importance than in Lee & Tweedie (1977). This is consistent with respondents' thoroughness of reading of these reports, shown in Table 4.

The lack of relationship between accounting background and thoroughness of reading and understanding of annual reports may be

explained by the close knowledge that members have of their co-operative. From their regular and frequent trading contacts, they may have developed significant accounting knowledge outside of formal training. That is, these co-operative members may have significant tacit knowledge. Keef & Robb (1994) found that tacit knowledge was independent of prior academic training.

This study found that there was a relationship between size of shareholdings and readership of annual reports. The reason for the difference may be cultural: the New Zealand 'do it yourself' ethos; that is, shareholders may make their own investment decisions without the use of an analyst. Therefore they need to read annual reports of other companies more thoroughly.

Conclusion

This study examined the reading and understanding of the annual report of a major New Zealand co-operative by its members. It found that the most thoroughly read sections of the annual report are the financial reports and the directors' report. All sections are read more thoroughly by members of the co-operative than by the private investors in Lee & Tweedie (1977). The most useful piece of financial information was the profit figure, which is consistent with Lee & Tweedie (1977).

However there were differences attributable to the different form of organisation and different characteristics of investors. Differing levels of importance were placed on sales/turnover, assets, rebates/dividends and the capital base. Readers focused on and read more thoroughly different parts of the annual report, especially the directors' report and the statement of cash flows.

This study has made a step forward in addressing the dearth of accounting-based research in co-operatives, and provides a foundation for further studies. However, the findings are not necessarily generalisable between countries and to other types of co-operatives, such as consumer co-operatives, agricultural produce co-operatives and credit unions. Therefore this research is being extended to a range of other types of co-operative, and internationally to the United Kingdom, Canada and the United States of America.

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Notes

- 1 As this study examines understanding and use of the whole of the annual report and other financial information, these content and readability studies are not reviewed in detail here.
- 2 It should be noted that the Co-operative Bank and the Co-operative Insurance Society do not report directly to members. Rather, they are wholly-owned subsidiaries of the Co-operative Group, which is accountable to its corporate and individual members. However, the commitment to a comprehensive interpretation of the concept of accountability is also reflected in reporting practices of the Co-operative Group.
- 3 The 109 voting members each held one 'B' membership share too.
- 4 These do not sum to 81% as some respondents ticked several boxes.
- 5 S157 of the UK Companies Act 1948 determined the content of the reports used by Lee & Tweedie's respondents.
- 6 These sum to more than 49 as some of the respondents ticked more than one category.
- 7 These sum to more than 35 as several respondents mentioned several pieces of information.
- 8 Dividends in Lee & Tweedie (1977).
- 9 Foodstuffs (SI) Ltd has set up a Community Trust which makes educational, community and compassionate grants to communities in the areas in which it operates.
- 10 The National Progress Report outlines the combined co-operative activities of the three Foodstuffs co-operatives throughout NZ.
- 11 The Foodstuffs' Directors' Report is signed by the Chairman, although there is not a section named Chairman's Report.
- 12 Funds Statement in Lee & Tweedie (1977).
- 13 In the Foodstuffs' report the statistical data is included in the Directors' Report.
- 14 Lee & Tweedie (1977) categories, Future prospects and Company development and expansion, have been combined into one category.

Appendix: The Questionnaire

1. How long have you been involved in the grocery business? years
2. How would you describe your business background and experience? *(Please tick whatever applies.)*
 - ☐ Accounting qualification *(state which)*
 - ☐ Courses in accounting
 - ☐ Basic bookkeeping experience
 - ☐ Management qualifications *(state which)*
 - ☐ Foodstuffs' training courses
 - ☐ Other qualifications *(state which)*
 - ☐ Directorships
 - ☐ Other *(please specify)*
 - ☐ None

3. What particular financial information about Foodstuffs is important to you?

*When completing the questionnaire,
it may be helpful to have a copy of the Annual Report on hand.*

4. Which sections of the annual report do you read, and how thoroughly do you read each ?
(Please tick appropriate columns.)

Section	Do not read at all	Read briefly for interest	Read thoroughly
Highlights			
Directors and Executives			
Directors' Report			
Foodstuffs Community Trust Report			
Corporate Governance			
Statutory Information			
Auditors' Report			
Statement of Financial Performance			
Statement of Movements in Equity			
Statement of Financial Position			
Statement of Cash Flows			
Notes to the financial statements			
National Progress Report			
Directory			

*If you answered 'Read thoroughly' to **any** category, please go to question 5.*

*If you answered 'Do not read at all' to **all** categories, please go to question 6.*

Otherwise, go to question 7.

5. *(For those who read thoroughly all or part of the annual reports)*
Do you undertake any form of analysis of the data contained in the reports? *(Please tick the appropriate box.)*
 - ☐ Yes
 - ☐ No

If yes, please specify what analysis you undertake:

Please go to question 7.

6. (For those who do not read the annual report at all)
Why do you not read the annual report?
7. What ranking of importance would you give to the following *purposes* of the financial statements in Foodstuffs' annual reports?

(1 = most important, 2 = next important, and so on; you may have equal rankings)

Purpose	Ranking
To make directors accountable to members	
To provide information for the Inland Revenue Department	
To give members an indication of the value of the company	
To give members an indication of the fair value of their shares	
To give members data useful for investment decisions	
To justify rebates to members	
Any other (<i>specify</i>)	

8. What ranking of importance would you give to the following *sections* of Foodstuffs' annual reports? (1 = most important, 2 = next important, and so on.)

Section	Ranking
Highlights	
Directors and Executives	
Directors' Report	
Foodstuffs Community Trust Report	
Corporate Governance	
Statutory Information	
Auditors' Report	
Statement of Financial Performance	
Statement of Movements in Equity	
Statement of Financial Position	
Statement of Cash Flows	
Notes to the financial statements	
National Progress Report	
Directory	

9. Do you have shares in any other company (either cooperatives or investor-owned firms)?
(Please tick the appropriate box.)

☐ Yes ☐ No

If yes, how many companies do you hold shares in?

- ☐ 1 – 5
☐ 6 – 10
☐ 11 – 20
☐ 20 +

10. Which of the following sources of information about companies do you read, and how thoroughly do you read each? *(Please tick the appropriate column.)*

Source	Do not read at all	Read briefly for interest	Read thoroughly
Companies' annual reports			
Companies' six monthly reports			
National Business Review			
The Independent			
Local newspapers			
Trade magazines			
Any other <i>(specify)</i>			

*If you answered 'Do not read at all' to **all** categories, please go to question 11. Otherwise, go to question 12.*

11. *(For those who do not read anything about companies)*
Why do you not read anything about companies?

Go to question 13.

12. *(For those who read about companies.)*
What particular information contained in any of the following sources do you find particularly relevant to you?

Source	Information
Six monthly financial reports	
National Business Review	
The Independent	
Local newspapers	
Trade magazines	

13. What do you understand by the following terms commonly used in financial reports?

Depreciation
Movements in equity
Current assets
Foreign currency translation reserve
Minority interests
Derivative financial instruments

14. Do you believe the financial information given in Foodstuffs' annual report is sufficient for members? *(Please tick the appropriate box.)*

☐ Yes ☐ No ☐ Don't know

15. Which of the following financial aspects of Foodstuffs are you able to realistically assess from the present type of annual report? *(Please tick the appropriate box.)*
- | | |
|--|--|
| ☐ Profitability | ☐ Capacity to survive |
| ☐ Managerial efficiency | ☐ Investment policy |
16. What financial data do you use to assess the above factors?
- | Factor | Data |
|-----------------------|------|
| Profitability | |
| Capacity to survive | |
| Managerial efficiency | |
| Investment policy | |
17. Is there any additional financial information which you think members should be given in Foodstuffs' annual reports? *(Please tick the appropriate box.)*
- ☐ Budgets
- ☐ Profit forecasts
- ☐ More details on human resources
- ☐ Environmental information
- ☐ Increased disclosure of existing information *(specify)*
- ☐ Other *(specify)*
18. Do you consider the financial results which are annually reported to you by Foodstuffs to be
- ☐ An accurate reflection of their financial progress and position
- ☐ An approximation of their financial progress and position
- ☐ An inaccurate reflection of their financial progress and position
- ☐ Other *(specify)*
19. Is there anything in particular in Foodstuffs' present annual report which could be presented more clearly? *(Specify briefly)*